DOMESTIC EFFECTS OF FOREIGN INVESTMENT.

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IT IS a pleasant but mistaken belief that a nation can have a democratic government at home and yet be tyrannical abroad or oppressive to other nations. The fate of foreigners and men of subject races seems to many to make no difference to housing or education or what is vaguely called by the benevolent "social reform." In actual practice, however, it should be plain that if some of us or our agents oppress foreigners or subject races, these oppressors will be more ready and more able to oppress "us." If we all join armies used for foreign conquest, we cannot expect foreigners to give up all thought of conquering us, and therefore we must live under arms, that is undemocratically. The foreign policy of a government thus affects very intimately the prospectsof domestic reform.

If the government is for the sake of all the governed, the results of its action must be good for all and not merely for a select group; and foreign policy, therefore, in support of foreign investment, if it is good, must be proved to have good results for all.

It is not well, however, to be indefinite about our conceptions of justice or of wealth and well-being. The interests of all are the interests of a number of persons of whom "the few" are some. The interests of the few are in foreign investment very obvious, but the interests of all are not. For this reason perhaps and not because of any ill-will, governments attend to the few who are vocal and certain of their purpose. The trouble is that the general well-being is not clearly expressed and is perhaps hardly conceived in definite terms. This general well-being must, however, be the criterion for judging of the action of governments in foreign policy. It will, therefore, be necessary to discover what are the good and bad effects of

foreign investment upon the people whose government supports the investor.

There are two distinct issues. One is the economic effect of investment abroad; the other is the effect, economic or political, of a foreign policy connected with this investment. The two cannot indeed in real life be disentangled; but it does not follow, if investment abroad is good for wealth, that foreign policy should, therefore, be guided by the investors.

Many results, some good, some bad, follow from foreign investment. It is sometimes argued that if taxation at home increases, capital will go abroad; but this may not be on the whole objectionable, and, if the capitalist would follow his capital, it might be a positive advantage; for a country needs most, not spenders, but workers. That, however, is too abstract an issue. The fact is that the investment of capital abroad may be an advantage to a country. For example, it tends to increase the trade and manufacture of the country from which the investments come. The reason is not economic, but psychological. Where British capital is invested, there is a tendency to use British local management and British organising ability; and from this follows a tendency to order British goods for the new enterprise. This effect, however, does not always follow. Capital from England invested, for example, in the United States may lead not to orders for British goods, but to orders for American goods. But indirectly it must come round to British exports of goods, or orders upon foreign goods to which British investors are entitled as interest. French capital invested in Russia did not much increase the French export to Russia. But on the whole, either directly or indirectly capital developing a new country increases the demand for goods in that new country. Capital invested abroad may therefore increase employment at home; and in some cases more employment than the same amount invested at home. For example, capital in Argentine railways may lead to orders for steel rails and locomotives, in the making of which many are employed,

whereas capital on a farm at home would employ a smaller number.

Secondly, it may be good for a country to receive income from investment abroad. If this income is ill-distributed the distribution may destroy all the good which might result from this income; but in the abstract the income is a payment for the service of providing capital, and this payment should have a good effect.

Thirdly, it tends, on the whole, towards peace if the interests of different nations are intertwined. Men who have property in another country do not desire that country to be ruined by war. Again, because the same enterprise may include some property in one country and some in another, the owner may begin to realise that many different countries have the same interests in producing goods and enjoying their use. The brotherhood of man is not so good a basis for peace as the common desire for boots; for it is easy to believe that a foreigner is not a man, but less easy to believe that he will not buy boots. It is good, therefore, politically for those at home if they do not have to arm to the teeth owing to the connection of some of their number with property in a foreign land. Hence rhetoricians sometimes oppose the connections of two countries through finance; for example, Clemenceau on 10th February, 1911, said in the Chamber of Deputies:

> "This new policy of *rapprochement* with Germany is born in financial circles. I do not wish to speak ill of financiers, but I believe that they are more at home in finance than in the foreign policy of France. They have no machine for weighing the imponderables—the sentiments, the passions, the ideas which make nations act. They see only what is saleable: and that is not enough." [1]

M. Clemenceau in 1911 evidently thought that financial connections would tend towards peace.

A foreign policy, developing or maintaining foreign investment, may for these reasons be in the interests of all the people, in spite of the fact that some gain directly and others indirectly, if at all, and in spite of the fact that some

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[1] *Journal Officiel.* 11th Feb., 1911.

gain very much more than others. But it must be understood that no general rule can prove that any particular investment should be supported by foreign policy. Each case has to be considered by making a balance of good and evil effects; for all that has been shown so far is that some maintenance of foreign investment may be beneficial. It is in that far good for the foreign policy of the country to be connected under the existing system of private property, with groups investing abroad.

The effects, however, of foreign investment upon the domestic situation may sometimes be evil. In the first place a people may be burdened with taxation to maintain armed forces for the defense or improvement of the property abroad of some of their fellow citizens. A classic example is the Boer War. The preparation for war and war itself may arise from foreign investment; and both of these are evil in the domestic sphere. If war must be prepared for, there must be less energy and less money, for more civilized activities. If war must be fought, the liberty of the individual, freedom of association, and a free press must all suffer.

The standard example of how expansion abroad for financial ends leads to confusion at home is to be found in the history of France during the activity of Jules Ferry from 1881 to 1885. In 1869 the Bey of Tunis had established a financial Commission on which there were a French inspector of finances, nominated by the French Government, and representatives of creditors, two delegates elected by the creditors of each of the three nations, France, Great Britain, and Italy. Tunis went bankrupt in 1870 which gave France an opportunity to intervene, and in 1884 the international Commission disappeared and France took over the debt and the resources of the country. The "success" in Tunis drove Italy into the arms of Germany and Austria, and French foreign policy thus consolidated the Triple Alliance against her. The result in France was an increasing expenditure on armaments and more waste of youth and brains in preparing for the inevitable war.

There are many examples of wars arising from foreign investment, the Boer War, the Spanish-American War, the Tripoli War, and the many small wars of France in Northern Africa. Clearly each war has many causes and it could not be reasonably argued that even the wars named were entirely or even mainly due to foreign investment. These wars, however, were partly due to the operations of those who controlled foreign investment upon the organisation of diplomacy and the tendencies in foreign policy. Their effects on the lands when the wars were fought may be omitted from the discussions here, for we are here concerned only with their effects upon domestic affairs.

The foreign investor sees a danger to his property or he sees a chance of improving the value of that property by the use of the power and wealth of his government. Perhaps he is cynical; perhaps he is simple-minded; but he manages somehow to identify the interests of his "country" with his interests in gaining more wealth, and the government, that is to say the political group in the ascendant at the moment as well as the officials, are easily persuaded that the interests of the country are at stake. Officials like to be important and politicians generally need something "showy" for advertisement. The newspapers live on crises. Commotion pleases everyone—at least for the moment. Thus the evils of war are endured by the mass of the people for the sake of the gain of a few.

The Boer War, for example, would generally now be regarded as having had evil effects upon the people of England; but the war was brought about largely through the operation of capital abroad. In the Transvaal there were the Eckstein group, Werner, Beit & Co., with capital investments in 1899 valued at over seventy-six million pounds. The Consolidated Goldfields Company of which Cecil Rhodes was a leading spirit belonged to this group. There were also J. B. Robinson with nineteen mines and fourteen millions of capital; and finally the Barnato firm.[2]

[2] Hobson, *The War in South Africa*, p. 191 sq.

These groups controlled the Press and gave to people in England highly coloured versions of what was going on. The advantages apparently in view of these interested groups were control of the labour market under a government more amenable than that of the Boers and perhaps an Imperial idea of aggrandisement and expansion of economic life in which they would be largest sharers. The war came about according to plan and the people of England paid the price.

That is what happens when foreign investments result in war; but this, of course, is exceptional. The evidence does not show that this is the normal result of foreign investment. Indeed war seems to result only when the investment is in a country with a weaker government than that of the investors. There have been many cases of default in the payment to investors in Europe by public authorities in the United States of America; but foreign policy has not yet led in such cases to war or the threat of war. It seems, therefore, that this evil result of foreign investment only can follow when the investment is placed in what are called "undeveloped" countries.

Another evil result of foreign investment may be the denuding of domestic enterprise or the defective development of domestic resources. If the pull of higher returns or investments is all that matters, then investments abroad may make investments at home too few.[3] The rate for capital at home rises as a result of the higher rates offered abroad and industry and employment at home are therefore diminished or are less than they might otherwise have been. There have been many complaints in France against the export of French capital on the ground that French industry is thereby weakened; and some have even suggested that the government should prohibit or limit the export of capital for this reason.[4]

Again, investment abroad sometimes ensnares the people abroad to the group of financiers at home, and this re-

[3] C. K. Hobson, *Export of Capital*, p. 37 sq.

[4] Lysis, *Contre l'Oligarchie financière.*

acts upon the domestic situation even when the financial group, having secured predominance then stands, and asks its fellow countrymen to stand, not for war, but for law and order.

It is unpersuasive to preach peace among nations if your income from rubber shares is raised by slave labour. It may be wrong to use force; but you cannot prove it if your wealth depends upon the subjection of other peoples to the force of your armies; and many pacific persons do not refuse to derive advantage from a situation which they condemn.

Again, the income from investments abroad comes not to the people as a whole, not to the state, as representing the people, but to a few. This tends to the enrichment of the few and perhaps to the greater difference between their wealth and the meagre incomes of the majority. It is, however, argued that the many gain as consumers, *e.g.*, cheaper food in consequence of investments in Argentina. But the enrichment gives to the small groups increased political power. They have the Press, the motor cars for election time, the ability to pay agents, the best means for forming and expressing the only vocal "will of the people." But the source of their wealth is unknown. Wealth got from foreign lands is generally wealth got in secret and absentee owners are often worse for the land they inhabit than for the land they own, but do not burden with their irresponsible expenditure.

A further result which may be thought in the main bad is that capital invested in enterprises in undeveloped countries may use labour there to undersell the products of labour in the more highly industrialised countries. Thus the cotton manufacture of India, using Indian labour, may in the end limit if not extinguish the Manchester cotton trade. The jute industry of India, itself the result of the investment there of British capital, may make it impossible to continue the jute industry in Scotland. A shipbuilding firm from the Clyde has recently moved its works to Vancouver partly, at any rate, to avoid labour difficul-

ties; and economists and literary men have already prophesied that the higher paid worker of Europe would be thrown out of employment as soon as it became practicable to use in industries negroes, the Chinamen or the Malays.[5]

Foreign investment may thus have the effect of degrading the standard of life of the majority of the wage-earners in the countries which export capital.

The Basis of Foreign Policy.

Foreign policy is already affected by partial and momentary judgments of the good and evil flowing from foreign investment. Although no large principles have been accepted generally, and although no principles at all seem to be permanent, the influence of governments has in fact been directed sometimes because of the known effects of foreign investment; but because each government is regarded as acting for the sake only of the people who directly influence it, the action of governments has been generally directed to preventing the export of capital. The interest in view is mainly that of the country which might export capital, not the interest of the undeveloped country or of the world at large: and therefore it is the effect upon the domestic situation which seems to be in the minds of those who regulate foreign investment.

Thus the French Government requires that no capital shall go abroad at any time without official registration and license. At one time, when foreign investment was a new phenomenon, it was totally prohibited; for it was felt that the capital so exported would be a loss to France; and even now the control by the French Government over French investment abroad is dominated by the crudest conceptions of the interests of France as a whole.

By a royal ordinance of 18th November, 1823, foreign *government* loans were permitted to be quoted on the Bourse.

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[5] Dr. Dillon in the preface to his book on the Peace Conference seems to advocate this use of cheaper labour; and Dr. Inge, Dean of St. Paul's, has recently urged that the danger of this cheap labour is a reason for lower wages in Europe.

A letter of the Minister of Finance of 12th August, 1873, confirms this ordinance and notes that the *Chambre syndicate* of the Bourse must inform the Ministers of Finance and of Foreign Affairs of any new issues of capital proposed. The official recognition of other foreign issues, not state loans, dates from an imperial decree of 22nd May, 1858; and the Minister of Finance in a letter of 16th October, notes that the government can veto any issue. Rules for the new issues are laid down by decree of 1880 and 1893; and Article 5 of the former runs— "The Minister of Finance may in any case forbid the dealing in any foreign security in France." In two ways, therefore, foreign investment is controlled by the French Government. First, the *Chambres syndicates* of the "agents de change" operate, in their rules for new issues, under a law which gives them power to exact certain conditions. Secondly, this Stock Exchange must inform the government of proposed new issues and the government may refuse permission.[6]

The French Government sometimes uses this right of veto on foreign investments for diplomatic bargaining. For example, in 1909 the Danish Government intended to raise the import duties on French wines, and the French Foreign Office thereupon threatened the Danish Government that if the duties were imposed no new Danish loans would be allowed to be quoted in Paris. Similarly, Sweden and Norway were granted leave for quotation of their new loans in Paris only on consideration that they lowered their duties.[7] In 1909 the Krupps obtained a contract for artillery for the Argentine in competition with a French firm, and therefore the French Government refused to allow in France the raising of the Argentine five per cent loan of that year.

In 1911 the French Government refused permission for the quotation of an Hungarian loan in Paris. The reasons were (1) the money was to pay for expenses due to the annexation of Bosnia-Herzegovina, and for military needs

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[6] Becque, *l'Internat. des Capitaux*. p. 112 sq.

[7] Becque, *op. cit.*, p. 182.

of the Triple Alliance and (2) French capitalists had felt themselves interfered with in Austria. In 1912, the French Government refused permission for a loan for Cuba. It was urged that Frenchmen injured in the Cuban revolution of 1895 had not yet been compensated. M. Poincaré, the President du Consul and Foreign Minister, said in the Chamber (3rd February, 1902) that "the Government unanimously agree that the interests of France should take precedence of the financial interest—whatever that may mean!" A Turkish loan in 1910 was refused quotation both because the young Turks were hostile to France and because the security was regarded as doubtful. This latter reason is similar to that given by the British Foreign Office to explain why certain loans to China would not be supported by the British Government; but the reply made by financiers in the both cases was that they were the best judges of the security for the loan; a reply which has never been fairly used by those who advocate or those who operate the governmental control of foreign investment.

In England the situation is different. The Committee of the Stock Exchange in London makes and enforces the rules for new issues and these rules make no distinction between conditions for admission of home and foreign securities. Ordinary Company Law, chiefly now the Companies Consolidation Act of 1908, governs the situation; but the government had no power to forbid any issue of foreign securities. The Foreign Office, however, does influence new foreign issues, as has been shown above in the case of the Chinese loans. All other countries follow this method of influence rather than control, and France, therefore, is an exception in having a definite and legal relation established between the Stock Exchange and the Foreign Office in regard to foreign issues.

During the War, however, the British Government, like other governments, extended its control over financial operations, and one of the first Regulations under the Defence of the Realm Act was to prevent the export of capital except by license. The text was as follows:

"A person resident in the U. K. shall not, without permission in writing from the Treasury, directly or indirectly, either on his own behalf or on behalf of any other person resident in the U. K.—

(1) Send any remittance out of the U. K. for the purpose of:

(a) making or subscribing to any loan or subscribing to any issue of capital outside the U. K.; or

(b) purchasing any stock, shares or other securities or any property other than merchandise, if the securities or property are not in the U. K.; or

(c) purchasing any foreign currency to be held with a view to appreciation in value or as an investment; or

(2) take part in, or agree or offer to take part in, any of the above mentioned transactions if such transaction involve the sending of any remittance out of the U. K." [8]

This regulation is now no longer in force; but it is interesting evidence of the tendency of war to separate the financial structure of the world into arbitrary units marked by political frontiers.

The same tendency is to be found in Germany. The Financial Secretary to the Treasury in the House of Commons, on 2nd March, 1921, said:

"The export of capital from Germany is prohibited by various laws of the German Government, the chief of which is the law of 26th June, 1918. I understand that the object of these laws is to prevent the evasion of taxes." [9]

All such action of government in regard to foreign investment is dominated by the idea of the national or *domestic* results of the investment. Control by a Treasury or a Foreign Office usually involves the attempt to separate and not to unite the peoples. Each government normally is considered by its people as the agent of their interest in contrast with the interests of foreigners, and the cry for control of foreign investments normally comes not from those who have large views of the interests of many different peoples but from those who desire to keep all available wealth for persons of their own nationality.

The tendency to separate the peoples, much increased

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[8] D.O.R. Regulation 41 D.

[9] *Hansard*, H. C., 2nd March, 1921, col. 1795.

by the war, is still more increased by the Treaties of Peace. In Section 297 of the German Treaty and Section 249 of the Austrian Treaty arrangements are made with regard to the property of German and Austrian subjects in the countries of the Entente. Part of such property consist of investments; and since these investments can be taken, under the Treaty, for the payment of monies owed by the German Government, there is naturally a discountenancing of foreign investment. After former wars the obstruction to intercourse was not so great; for now if the Peace Treaties are to be guides to the future the people of every nation will fear to invest any capital in any State with which their own may at any time quarrel; and presumably foreign policy will not support this giving of hostages to a possible enemy.

Problems are already arising. Owing to the rate of exchange with Europe, Canada is being severed more completely in finance from the United Kingdom and bound more closely to the United States. The foreign debt of Canada, governmental and private, amounts to about £800,000,000; about half of which is owing to British investors, but the United States citizens have increased the amount owed to them by Canadians since 1914 five times and they now hold about £250,000,000 of Canadian securities. This, undoubtedly, was one of the influences leading to the appointment of a Canadian governmental representative in Washington, in addition to the British Ambassador. What, then, are we to expect? Are we to refuse to Canada the use of American capital when she cannot obtain any from Great Britain, or are we to compel British citizens to invest in Canadian and not in French or Austrian enterprises? Are we to care at all from what source our investors draw their income? Or are we to refuse them permission to draw any income from abroad?

Clearly we must at least refer to the effect upon the country in which we live if we are to decide upon the action of government or the position to be given to financiers and investors.

A foreign policy, therefore, which supports foreign in-

vestment will be partially the cause of all the goods which flow from such investments, and the balance cannot easily be struck. The agent of the state and the people as the "principals" in foreign policy will have to decide upon the course to follow, whether or not to support any particular foreign investment, after making some estimate of the good and the evil which is likely to be the result. That may indeed be difficult to do; but it is most important at the moment that it should be generally recognized that a judgment should be made. Investments go abroad. Results follow at home. Politicians and the foreign services are called upon to act in the matter; and unless there is some popular understanding of the importance of such problems, policy becomes a mere drift,—an opportunism without moral quality on economic or political value.

Further, whatever the action of government, either by control, or by support of foreign investment, it is important to notice that the activities of governments play comparatively a small part in this financial world. The movement of capital abroad is in the main directed by no conception of public service, however crude, but by an appetite for private gain. In so far, therefore, as investment abroad has any effects, good or evil, upon domestic affairs, the effects are chiefly due to the use of private property for private gain, and not to the action or inaction of governments. Thus we appear to face a dilemma. Unregulated foreign investment is dominated by the idea of private gain and may have very pernicious public effects; and on the other hand, regulation of foreign investment by governments seems to lead only to the separation of nations and the domination of the most selfish and nationalistic foreign policy.

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